

Message Text

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ACTION SS-25

INFO OCT-01 ISO-00 SSO-00 /026 W
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O 222053Z AUG 78
FM AMEMBASSY SANTO DOMINGO
TO SECSTATE WASHDC IMMEDIATE 5768

C O N F I D E N T I A L SECTION 1 OF 2 SANTO DOMINGO 4605

EXDIS

EO 11652 GDS
TAGS: EGEN, DR
SUB: ECONOMIC PROSPECTS FOR THE DOMINICAN REPUBLIC-IMF AND WORLD
BANK VIEWS

REF: STATE 198898,

1. EMBASSY APPRECIATES OPPORTUNITY TO COMMENT ON IMF/IBRD VIEWS
REF DR'S ECONOMIC PROSPECTS. WE CERTAINLY AGREE THAT A PROBLEM
EXISTS, AND THAT MATTERS WILL GET WORSE BEFORE THEY GET BETTER.
THE KEY QUESTIONS RELATE TO THE SEVERITY OF THE PROBLEM, AND THE
NEEDED MIX OF REMEDIAL MEASURES.

2. WE ESTIMATE THAT THE DR WILL CLOSE OUT 1978 WITH A TRADE
DEFICIT OF \$210 MILLION (EXPORTS \$640 MILLION; IMPORTS \$850) AS
OPPOSED TO THE \$67 MILLION DEFICIT REGISTERED IN 1977. THIS RE-
FLECTS GENERALLY LOWER COMMODITY PRICES FOR EXPORTS AND AN UN-
CHANGED IMPORT PICTURE.

3. SPECIFICALLY, WE SEE KEY 1978 EXPORTS AS FOLLOWS:

SUGAR: \$205 MILLION (DOWN FROM \$249 MILLION IN 1977)

COFFEE: \$110 MILLION (DOWN FROM \$186 MILLION)

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CACAO: \$ 80 MILLION (DOWN FROM \$93 MILLION)

FERRONICKEL: \$ UP MILLION (DOWN FROM \$91 MILLION)

BAUXITE: \$ 23 MILLION UP FROM \$22 MILLION)

GOLD AND SILVER: \$ 65 MILLION (UP FROM \$60 MILLION)

TABACCO: \$35-40 MILLION (UP FROM \$29 MILLION)

4. ALTHOUGH WE HAVE NOT ANALYZED PROSPECTS FOR 1979 AND BEYOND, WE WOULD EXPECT SOME REBOUND IN CYCLICAL EXPORT MARKETS, WITH AT LEAST PARTIAL RECOVERIES IN SUGAR AND FERRONICKEL. TOURISM, WHICH HAS BARELY SCRATCHED THE SURFACE OF ITS POTENTIAL, SHOULD CONTINUE TO GROW. GOLD EXPORT WILL INCREASE AS SOON AS THE LAS CACAOS CONCESSION IS AWARDED; THERE IS ALSO STRONG U.S. INTEREST IN SEVERAL OTHER GOLD EXPLORATION/EXPLOITATION CONCESSIONS. NEVERTHELESS, IMPORTS WILL NO DOUBT INCREASE REFLECTING EXPECTED PRICE INCREASES ON OIL AS WELL AS FINISHED GOODS, AND THE END RESULT IN 1979 MAY WELL BE AS BAD AS, OR WORSE THAN, 1978.

5. IMPORTS, WHICH SLOWED DRAMATICALLY AFTER THE MAY 16 ELECTIONS, ARE IN PART FINANCED IN ADVANCE BY THE PARALLEL MARKET. OVER THE PAST SEVERAL MONTHS, THE CENTRAL BANK HAS INCREASED THE LIST OF IMPORT PRODUCTS FOR WHICH OFFICIAL EXCHANGE IS NOT AVAILABLE, AND WHICH THEREFORE MUST RESORT TO THE PARALLEL MARKET. IN SUBSTANCE, THIS IS WHAT IS BEING RECOMMENDED BY THE IMF/IBRD. CENTRAL BANK ESTIMATES THAT SOME 40 PERCENT OF IMPORTS ARE CURRENTLY UTILIZING THE PARALLEL MARKET FOR 1978.

6. IN THE PERCEPTION OF THE GODR, THE PARALLEL MARKET IS NOT SIMPLY "TOLERATED" AS INDICATED PARA 2 REFTL. IT IS A SEMI-OFFICIAL, GOVERNMENT-SANCTIONED TOOL ACTIVELY UTILIZED BY THE CONFIDENTIAL

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GODR TO IMPLEMENT ITS POLICIES REGARDING ALLOCATION OF SCARCE FOREIGN RESERVES. THE PARALLEL MARKET RATE HAS VACILLATED IN A BAND OF 18-22 PERCENT OVER THE OFFICIAL PARITY DURING THE PAST FEW YEARS, WITH DRAMATIC SHIFTS (SUCH AS TO 30 PERCENT IN THE WAKE OF MAY 16) THE EXCEPTION RATHER THAN THE RULE. SINCE THEN THE RATE HAS BEEN EASING BACK DOWN TO THE TRADITIONAL BAND AND IS CURRENTLY AT 25 PERCENT.

7. AS A SUBSTANTIVE MATTER, THERE IS UNANIMITY AMONG DR ECONOMISTS THAT A "UNIFIED EXCHANGE MARKET" (WHICH IS TERMED DEVALUATION HERE), WOULD HAVE AN UNNEEDED AND INTOLERABLE INFLATIONARY IMPACT AS IMPORTS INCREASED IN PARICE (THE IMPORT MARKET IS FAIRLY INELASTIC), WHILE DECREASING EXPORT EARNINGS ON THE VAST BULK OF DOMINICAN EXPORTS WHOSE EXPORT VOLUME IS UNRELATED TO DOMINICAN PRICING (I.E., WHEN PRICES ARE SET IN THE INTERNATIONAL MARKET-PLACE). THE POTENTIAL FOR INCREASED MANUFACTURED GOODS EXPORTS AFTER DEVALUATION IS UNAPPEALING IN THE SHORT AND MEDIUM TERM TO A COUNTRY WITHOUT THE INSTALLED CAPACITY, TECHNOLOGY, AND MARKETING KNOWLEDGE.

8. THE GUZMAN ADMINISTRATION IS GOING TO HAVE MORE THAN ITS SHARE OF UNPOPULAR YET NECESSARY ECONOMIC MEASURES TO DECIDE ON,

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C O N F I D E N T I A L SECTION 2 OF 2 SANTO DOMINGO 4605

EXDIS

EO 11652 GDS
TAGS: EGEN, DR
SUB: ECONOMIC PROSPECTS FOR THE DOMINICAN REPUBLIC- IMF AND
WORLD BANK VIEWS

INCLUDING THE RAISING OF ELECTRIC RATES AND TELEPHONE RATES.
IF CURRENTLY WIDESPREAD REPORTS ARE ESSENTIALLY ACCURATE, GUZMAN
MAY FIND THAT HIS FIRST TASK IS TO REPLACE THE DESKS, TYPE-
WRITERS, VEHICLES, ETC. OF GOVERNMENT AGENCIES. REMOVED BY
DEPARTING INCUMBENTS. ONE POINT STANDS OUT CLEARLY AS GENERALLY
ACCEPTED GOSPEL: IF GUZMAN MAKES WAVES, HE'LL BE THE FIRST TO
DROWN IN THEO. THE MILITARY/BALAGUERISTA/REFORMISTA FORCES
WILL BE EXAMINING THE NEW ADMINISTRATION'S DECISIONS MICROSCOPICALLY, LOOKING FOR SIGNS OF UNACCEPTABLE RADICALISM. THUS,
IT WOULD APPEAR THAT THE OUTSET OF GUZMAN'S ADMINISTRATION
WOULD BE PARTICULARLY DIFFICULT POLITICALLY FOR A MEASURE AS
DRASTIC AS DEVALUATION.

9. FROM OUR PRELIMINARY DISCUSSIONS WITH THE NEW GOVERNMENT
WE ARE REASONABLY CONFIDENT THAT GODR ARREARAGES TO USG (E.G.,
EXIMBANK, FMS) WILL BE CLEARED UP ON A PRIORITY BASIS.
THE DR WILL PROBABLY SEEK RE-FINANCING OF DEBT TO
COMMERCIAL BANKS, WHICH WOULD BE WELCOMED BY SEVERAL OF THE BANKS.
PRIVATE BORROWING IS AVAILABLE FOR THE ASKING (WE ESTIMATE THE
READY AVAILABILITY OF AT LEAST \$200-\$300MILLION), THOUGH AT
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HIGHER INTEREST RATES THAN OFFERED BY THE IFI'S. SUCH BORROWING, OR BORROWINGS FROM IFI'S WOULD CERTAINLY INCREASE THE DEBT SERVICE RATIO, WHICH WE NOW ESTIMATE AT 8.8 PERCENT, BUT WOULD NOT RESULT IN AN INTOLERABLE SITUATION. FROM OUR DISCUSSIONS WITH LOCAL U.S. BANKERS, THE RECENT PERIOD OF NON-PAYMENT APPEARS GENERALLY ACCEPTED AS A POLITICALLY-BASED ABERRATION IN THE "SLOW BUT STEADY" DR PAYMENT TRADITION.

10. WE CERTAINLY AGREE WITH THE NEED FOR A COMPREHENSIVE DEVELOPMENT AND INVESTMENT PLAN, AS WELL AS WITH ADDED EMPHASIS ON EXPORT-ORIENTED INVESTMENT INCENTIVES. CONSIDERATION IS BEING GIVEN BY SOME GODR OFFICIALS TO NARROWING FURTHER USE OF LAW 299 (THE IMPORT SUBSTITUTION LAW) THROUGH REGULATION; THIS APPEARS MORE PALATABLE THAN OUTRIGHT REPEAL.

11.. WHILE PRESIDENT BALAGUER'S ANTIPATHY TO FOREIGN BORROWING WAS EXTREME (HE EQUATED IT WITH THE PROBABILITY OF FOREIGN OCCUPATION, AS IN 1916-24), THERE ARE FEW NATIONAL ECONOMISTS WHO REGARD BORROWING AS THE LONG-TERM SOLUTION TO THEIR PROBLEMS. LIKEWISE, DEVALUATION AND/OR THE ABOLITION OF THE PARALLEL MARKET IS NOT ACCEPTED AS VIABLE BY THE NEW ADMINISTRATION'S LEADERS. RATHER, ATTENTION WILL BE FOCUSED ON INCREASED AGRICULTURAL OUTPUT AND EXPORTS RESULTING FROM ADDED IRRIGATED LANDS AND AGRICULTURAL POLICY IMPROVEMENTS, NATURAL RESOURCE EXPLOITATION, TOURISM, EXPORT INDUSTRIES IN THE FREE ZONES, AND CONTINUED (THOUGH PERHAPS MORE CLOSELY REGULATED) ATTRACTION OF FOREIGN PRIVATE CAPITAL INVESTMENT.

12. SERIOUS CONSIDERATION IS BEING GIVEN BY THE DR'S LEADING ECONOMISTS TO FORMALIZING, CONTROLLING, AND EXPANDING THE USE OF THE PARALLEL MARKET. UNDER THIS PLAN, COMMERCIAL BANKS WOULD BE PERMITTED TO PARTICIPATE IN THE PARALLEL MARKET, BRINGING TO IT ADDED STABILITY AND A BROADER BASE. NON-CONFIDENTIAL

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TRADITIONAL EXPORTS WOULD BE ALLOWED TO BENEFIT FROM THE PREFERRED EXCHANGE RATE, AND TOURISTS TO THE DR WOULD BE ELIGIBLE AS WELL. THE EMBASSY BELIEVES THAT THIS TYPE OF STEP WOULD BE ECONOMICALLY LOGICAL, POLITICALLY VIABLE, AND HELPFUL IN MEETING IMF-IBRD REQUIREMENTS.

13. IN SUM, WHILE THE DR'S LONG-RANGE OUTLOOK IS DECIDEDLY POSITIVE, THE CONFLUENCE OF LOW SUGAR PRICES, HIGH OIL PRICES, AND DOMINICAN ELECTIONS, COMING AT A TIME WHEN THE DR'S POTENTIAL IN AGRICULTURE, TOURISM AND NATURAL RESOURCE EXPLOITATION HAVE YET TO BE REALIZED, WILL RESULT IN SOME LEAN YEARS ON THE HORIZON. TO BAIL ITSELF OUT OF ITS CURRENT PROBLEM, THE DR WILL BE SEEKING THE ASSISTANCE OF THE IBRD, BID, AND WOULD LOVE TO TAP IMF AS WELL, THOUGH NOT AT THE COST OF DEVALUATION.

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